



## Budget Tidbits... just the facts

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Budget Brief #4: (4/10/09)

### Proposals for Structural Reform

*Ten steps lawmakers still can take to put Olympia on firmer footing*

*"I'm concerned when you've been asleep for 78 days, it's hard to wake up in the last 27."*

*-- Rep. Brendan Williams, D-Olympia<sup>1</sup>*

#### **I. A Session of Missed Opportunities?**

Since before the 2009 session began, Senate Republicans have been advocating for a three-pronged approach to the budget:

- (1) Take early action to compound savings;
- (2) Make structural reforms; and
- (3) Look at reductions in programs.

Budget writers, and the Legislature, do a disservice to the public by skipping over the structural reforms component. It opens up a distrust with the public, which demands -- rightfully so -- that every rock be overturned. And that simply has not occurred.

**Below are ten ideas for structural reform -- with accompanying legislation -- that the Legislature would do well to implement in the waning days of this session,**

ranging from big to small, from higher education access to funding for developmentally disabled youth, from reforming basic health plan eligibility to pension policy changes, from a constitutional amendment requiring saving extraordinary revenue growth to helping new businesses survive by eliminating the B&O tax during the first two years.

Each helps with the current budget situation, but even more importantly, each bill puts state government on better footing by making long-lasting reforms in areas of need.

## **II. Ten Legislative Proposals for Structural Reform**

### **1. Higher Education Access (Senate Bill 6156)**

The proposed Senate budget cuts enrollments from current budgeted levels by over 3,200. However, such enrollment reductions are not necessary. It is possible to maintain -- and actually increase -- budgeted enrollments through policy changes.

SB 6156 proposes:

- Limiting Tuition Waivers --- Higher education institutions grant more than \$400 million of tuition waivers per biennium, only a tiny fraction of which are issued for financial need reasons.<sup>2</sup> Requiring institutions to reduce the amount of tuition they waive by 10% would generate enough revenue to fund 3,760 additional enrollments, more than offsetting the proposed Senate enrollment reduction.<sup>3</sup>
- Eliminate Subsidy of Career Students -- The state provides a taxpayer subsidy for students, regardless of how long they have been enrolled. Most recent data showed there were over 1,500 students at the four-year institutions who had in excess of 125% of the credits needed to complete their degree.<sup>4</sup> Eliminating the state subsidy for these students, subject to an appeal process, would incentivize timely graduation and open access to incoming students.
- Other Reforms -- The bill also requires institutions to maintain current in-state enrollment ratios to take away an incentive to enroll more out-of-state students to the detriment of in-state students; establishes goals to increase distance-learning enrollments; increases charges for adult basic education; and authorizes institutions to charge differential tuition for upper-division courses that are significantly more expensive to offer.

### **2. Basic Health Plan Eligibility Reform (Senate Bill 6154)**

The Senate and House both propose saving \$250 million in the Basic Health Plan, yet suggest no statutory reforms to the program. The Senate budget contains language authorizing disenrollment of people above 100% of poverty level to achieve savings.<sup>5</sup>

There are better ways to achieve savings, namely by transforming eligibility for the program. Popularly conceived as a health plan for low-income uninsured citizens, there is no requirement an enrollee be a citizen, be uninsured, or be poor. SB 6154 would add these requirements to eligibility for the Basic Health Plan:

- Citizenship -- The enrollee must be a United States citizen or legally admitted for permanent residence. Data suggests tens of thousands of non-citizens are on the Basic Health Plan currently;<sup>6</sup>
- Asset Test -- Liquid assets of the enrollee's family must not exceed an amount established by the Health Care Authority administrator in rule;
- Waiting Period -- A 2006 study found that 45% of BHP enrollees had insurance at the time of enrollment, choosing to drop their coverage for the cheaper BHP.<sup>7</sup> The bill requires a waiting period of four months without private insurance before being eligible to be enrolled in the Basic Health Plan. The waiting period is waived if the applicant has a serious medical condition.

These three reforms would ensure the program targets low-income, uninsured citizens.

### **3. Developmentally Disabled Youth or Movie Tax Credit? (Senate Bill 6153)**

In 2006, the Legislature, under legislation prime-sponsored by Sen. Lisa Brown, passed a \$7 million per biennium tax credit for businesses that make donations to the Washington motion picture competitiveness program.<sup>8</sup>

In terms of priorities, isn't there a better use of tax policy and services?

SB 6153 would delete contributions to the motion picture competitiveness program as an eligible tax credit, replacing it with a tax credit for businesses that make contributions to the supported employment services program which assists with the transition of developmentally disabled youth to the workforce after graduating high school.

The Senate budget does not provide funding for these developmentally disabled youth. Advocates estimate that employment services to over 1,000 developmentally disabled youth could be provided with the \$7 million.

The proposal is budget-neutral.

### **4. General Assistance-Unemployable Reform (Senate Bill 6155)**

General Assistance-Unemployable is a state-only program which provides cash and medical benefits for the "temporarily unemployable". Washington is one of only 19 states with such a program and the only one in the Northwest. Despite being a program of temporary assistance, there is no time limit on receipt of benefits. It is one of the fastest-growing areas of the state budget.

Some facts about GA-U:

- Caseloads have nearly tripled in eight years -- growing from 10,610 in July 2003 to over 30,600 forecast for June 2011.<sup>9</sup>
- This is over 14 times as fast as population growth in Washington over that time.
- The program's costs are expected to exceed over \$400 million next biennium, or the equivalent of state support for Western Washington University, Eastern Washington University, Central Washington University, and The Evergreen State College combined.
- GA-U clients are largely working-age adults without dependents: 78% are between 25-54; 75% are white; and 59% are males. The most prevalent treatment was for depression (44%).<sup>10</sup>
- A sizable number of GA-U clients get arrested: 23% of clients had been arrested in the last year, and 54% had been arrested in the last ten years. A 2007 study found the 14,300 clients at the time had been arrested on 133,161 different charges over the prior ten years.<sup>11</sup>

SB 6155 would make two substantive reforms to the program: one, it would place a time limit on state assistance (those who are long-term disabled are eligible for federal coverage); and two, standards for being "unemployable" would align with the federal standards, rather than the more generous standards currently utilized.

This would bring the program in line with its intent as a program of temporary assistance, slow the extraordinary growth, and free up valuable taxpayer funds for higher priorities such as education and services for senior citizens and the developmentally disabled.

It is expected these reforms would save over \$250 million, more than either budget proposal.<sup>12</sup> And unlike the amorphous savings in the Senate and House budgets on GA-U, these changes would bring long-term reform to the program.

## **5. Competition Council -- Providing Services Cost-Effectively ([Senate Bill 5409](#))**

In 2002, the Legislature approved competitive contracting as a way to ensure services were being provided in the most efficient and cost-effective way possible. Those provisions have not been utilized.

SB 5409 would establish a Competition Council, a 15-member group, that would evaluate the privatization potential of activities performed by state government and annually make recommendations on services that may be able to be provided more cost-effectively. Following the council's recommendation, the governor would direct the agency to pursue a contract using the competitive contracting procedures first adopted in 2002.

## **6. Business & Occupation Tax Exemption for New Businesses ([Senate Bill 6057](#))**

Washington has the highest business failure rate in the country.<sup>13</sup> And one of the largest obstacles for new businesses is the business and occupation (B&O) tax, which is paid regardless of whether a business is profitable.

SB 6057 addresses this long-standing issue. It would provide a two-year exemption from the B&O tax for new businesses with less than 25 employees, plus such businesses would receive a 50% discount in their third year of existence. Additionally all new businesses, regardless of size, would receive a one-year exemption from B&O taxes. This would provide an incentive for businesses in other states to consider locating in Washington, adding a needed tool to the state's economic incentive toolbox.

The Department of Revenue estimated over 90,000 businesses would benefit over the four-year time frame of the exemption.<sup>14</sup> Costs would be \$11 million in 2009-11 and \$32 million in 2011-13. Repealing the sales tax exemption on hybrid cars would more than offset the cost of this proposal in the 2009-11 biennium and largely offset the four-year impact.

## **7. Bilingual Education (Utilize [RCW 28A.180.080](#))**

One of the fastest-growing programs in state government is bilingual education, with enrollment growing at ten times the rate of basic K-12 education, far in excess of what census projections indicate should be the rate of growth. Program costs have grown by two-and-a-half fold in the last dozen years.<sup>15</sup> Districts receive an enhanced rate of \$934 per student for each bilingual student which continues for as long as the student is classified as a bilingual student (meaning the funding goes away when the student transitions to a regular classroom).

Statistics indicate bilingual children are being ill-served by the current structure and delivery of service:

- Only 15% of students successfully transitioned to a regular classroom last year.
- 37% have been in the program for more than 3 years. This is quadruple the level twenty years ago, when only 9% were in program more than 3 years.
- 14% have been in the program for more than 5 years.
- Most staff instruction is provided by instructional aides, rather than by teachers.<sup>16</sup>

The system needs to be reformed to better serve these children. The financial incentive for districts to retain students in bilingual classification needs to be removed, and the state should make funding contingent upon instruction being given by certificated teachers, rather than instructional aides. RCW 28A.180.080 already sets in place the standard that the state will not fund a pupil for more than three years of bilingual education; however, the state budget funds districts regardless of length of stay, and it

serves no one well when the number of students in the program for longer than three years has quadrupled, especially when much of the increased length of stay could be attributable to not receiving instruction from a state certified classroom teacher. Savings range between \$25 and \$60 million short-term with even larger savings -- and better educational outcomes for children -- long-term.<sup>17</sup>

This inefficient and ineffective approach to bilingual education must stop.

#### **8. Pension Policy -- Defined Contribution Model ([Senate Bill 6045](#))**

Both legislative budget proposals fail to make actuarially-recommended contributions to the state's pension system, "saving" several hundred million dollars. These obligations are a contractual right, however. It is a "pay now or pay more later" system.

This will represent the third biennium in the past four biennia that the state will not have made the recommended contributions, putting the state at risk for a lawsuit for failing to fund the pension system in a sound and systematic manner. The state has a projected unfunded liability of over \$6 billion in its oldest retirement plans.<sup>18</sup> And the amount of funding the Legislature puts in each biennium is subject to substantial fluctuations.

Senate Bill 6045 proposes to put new employees (hired after Dec. 31, 2011) into a defined contribution plan, akin to what higher education faculty in Washington have -- and which faculty overwhelmingly choose over the state's existing defined benefit plans. The plan would require employees to put 5% of their salary toward retirement up to age 35; 7.5% up to age 55; and up to 10% thereafter. The state would provide matching funds up to 6%, far more generous than most private-sector employers. Employees would have the full range of state investment board options to invest in, have full portability, and have access to life-cycle options.

This would permit stability and predictability toward funding. Politics would be removed. As it should be.

#### **9. Pension Policy -- Preserve Full Funding Status ([Senate Bill 6046](#))**

As noted above, the state's oldest pension plans are underfunded. But as recently as two years ago the state's Law Enforcement Officers' and Fire Fighters' (LEOFF) plan 1 was fully funded, sitting at 114% market value. Sadly, that is no longer the case as the plan at last look was projected to be 86% funded, or equivalent to a \$734 million deficit.<sup>19</sup>

Part of the problem is that there is no statutory mechanism to "secure the surplus" and preserve fully-funded status. The State Investment Board is simply directed, regardless of a plan's funded status and closed/open enrollment status, to maximize return at a prudent level of risk.

SB 6046 would require the state actuary to report on the funded status of each of the state's closed plans (meaning plans where no new enrollees are allowed in). And when the actuary determined that on a market value, the plan was fully funded (meaning it had enough assets to pay off projected liabilities), the actuary would notify the state investment board. From there, the state investment board would be directed to establish investment policies to preserve the fully-funded status of the plan.

This would ensure that a closed plan, once fully funded, remained that way.

#### **10. Put Extraordinary Revenue Growth into Rainy Day Fund ([Senate Joint Resolution 8209](#))**

Senate Joint Resolution 8209 would require revenues exceeding 133% of the historical ten-year revenue growth to be put into the constitutionally-protected rainy day fund, rather than be spent.

Had this measure been in place earlier, today's budget problem would have been roughly \$5 billion smaller than it is today (\$2.4 billion more in savings, and the same amount that would not have been spent).

Passed by the Senate 41-7, the bill awaits action in House Appropriations. ***The bill is co-sponsored by Democratic Senate Majority Leader Lisa Brown, and it represents probably the single greatest reform available this session to prevent such a deficit in the future.***

### **Bottom Line**

Should the Legislature enact these reforms to put state government on more solid footing?

1. "New State Taxes? Clock is Ticking on that Answer." (The Olympian, 4/5/09).
2. Ways & Means staff analysis (4 year institution waivers: 11% financial need, 52% graduate students, 12% merit, 2% veterans, 7% non-residents, and 16% other).
3. Ways & Means staff analysis (2,165 enrollments at 4 year institutions and 1,615 at 2 year institutions).
4. OFM Education Data and Research Center (Jan. 16, 2009 presentation to Senate Higher Education Committee, p. 27).
5. PSSB 5600, sec. 214.
6. While there is no citizenship requirement, thus making a determination of how many non-citizens are on the plan difficult, monthly enrollment data suggests a sizable number of enrollees are probably not citizens. Enrollment reports indicate the subscribers' preferred language of communication, which is voluntarily disclosed. There were over 13,700 enrollees in March 2009 whose preferred method of communication was Spanish. There were an additional 42,000 who did not report their language of preference. Additionally, while there are 75,000 individual enrollees, there are also 27,000 "non-provider sponsor" enrollees. A non-provider sponsor is a group who goes and seeks out minorities or hard to reach populations and signs them up for the BHP. The group sends in the application for the individual and the Health Care Authority sends the organization a bill for the group's premium costs. The three largest non-provider sponsors of state subsidized enrollees are: Mt. Adams Foundation (13,432), located in Yakima; El Centro De La Raza (5,495) and the Leah Layne Foundation (3,328), located in Royal City where the population is 78% Hispanic. Statewide, Yakima County has the 2nd highest enrollment in the Basic Health Plan, exceeding such larger counties as Pierce, Snohomish and Spokane counties.
7. "Basic Health Plan Study, Part II: Who is enrolled? What services do they use?" Nov. 2006, JLARC
8. 2SSB 6558 (2006).
9. March 2009 Caseload Forecast Council data for non-GA-X caseload (includes GA-A, B, D, I, and R).
10. "GA-U Clients: Challenges and Opportunities", DSHS Research and Data Analysis Division (Aug. 2006)

11. "Arrests Among Working-Age Disabled Clients", DSHS Research and Data Analysis Division (Sep. 2007)
12. Ways & Means staff analysis indicates 6 month time limit savings in bill would save \$220 million, while the unemployable standards change would save \$110 million. There is likely overlap between the two, hence the \$250 million estimate.
13. "2007 Puget Sound Prosperity Report," Puget Sound Research Council (November 2007)
14. DOR staff (2/11/09), representing unique count of taxpayers over period exclusive of existing small business B&O tax credit.
15. LEAP (\$65 million in 1997-99 vs. \$164 million proposed in 2009-11 Senate budget)
16. "Educating English Language Learners in Washington, 2007-08" OSPI Research (Dec. 2008). On an FTE basis, there were 493 teachers and 565 instructional aides involved in bilingual instruction in 2007-08. On a headcount basis, the disparity is even worse: 819 teachers and 1,555 instructional aides.
17. Savings calculated based on estimates of state funding for districts of students receiving bilingual instruction for greater than five years (\$25 million) and greater than three years (\$60 million).
18. "State owes pension plans," Olympian (2/9/2009).
19. State Actuary analysis (1/24/2009).